No. 2653

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT.

A. R. TITLOW, as Receiver of the UNITED STATES NATIONAL BANK OF CENTRALIA, and the UNITED STATES NATIONAL BANK OF CENTRALIA,

Appellants,

vs.

ANNA E. McCORMICK,

Appellee.

BRIEF OF APPELLANTS

Upon Appeal from the United States District Court for the Western District of Washington, Southern Division.

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STATEMENT.

In August, 1913, the plaintiff, Mrs. McCormick, purchased of the United States National Bank of Centralia some $15,000.00 worth of school district warrants. After the purchase, she returned these warrants to the bank for collection (Tr. of R. 30). On February 4, 1914, a number of the warrants being called for payment, the bank forwarded them to the county treasurer and received in payment a check of $1,747.04. The check was drawn on Coffman, Dobson & Co., bankers at Chehalis, Washington, and was payable to the United States National Bank (Tr. of R. 30). On April 14, the balance of the warrants being called, the bank forwarded them to the county treasurer and received four additional checks, all payable to the order of the United States National and signed by the treasurer of Lewis County. The five checks thus received by the United States National in exchange for the warrants took three different courses.

1. *The Coffman Dobson Check.* This check (Exhibit 5, p. 33) for $1,747.04 was drawn on Coffman, Dobson & Co., bankers, payable to the United States National Bank, indorsed by it and sent in remittance of February 6th, containing other items amounting to $3,329.38, to Coffman, Dobson & Co. for credit account U. S. National (58).

The state of the account between Coffman, Dobson & Co. and the U. S. National *after* this remittance on February 6th, showed that Coffman, Dobson & Co. owed the U. S. National a balance of $5,046.20. From that day forward to February 14, 1914, Coffman, Dobson & Co. owed the U. S. National Bank as follows:

February	7,	$6,053.43
"	8,	Sunday
"	9,	1,921.59
"	10,	798.68
"	11,	1,067.53
"	12,	Holiday
"	13,	2,264.33

On February 14, the credit of the U. S. National with Coffman, Dobson & Co. *was entirely wiped out. On that date the U. S. National Bank owed the Coffman Bank* $489.80 (59). During the period from February 6 to February 14, the Coffman Bank was a correspondent of the U. S. National, and all checks which the Coffman bank cashed on the U. S. National and other Centralia banks were charged to the account of the U. S. National by the Coffman bank, and all checks which the U. S. National cashed on the Coffman bank were charged to the Coffman Bank's account with the U. S. National, so that the credit which the U. S. National had with Coffman, Dobson & Co. during that period was utilized by the payment of creditors and depositors of the U. S. National. (59).

The credit with the Coffman bank was exhausted by the U. S. National by the payment of checks by Coffman, Dobson & Co., which were drawn on the U. S. National and other banks. None of the checks or items which exhausted this account were drawn on reserve agents of the U. S. National (64), and no drafts of the U. S. National were cashed by the Coffman bank during that period. (66)

2. *Chehalis National checks.* Two checks (Exhibits 3 and 4, pp. 31 & 42), aggregating $8,974.18, were drawn by the county treasurer on the Chehalis National Bank and payable to the U. S. National, and indorsed and deposited by it in the Bank of California at Tacoma. These checks were received by the U. S. National on April 15 (61) and were forwarded by that bank to the Bank of California in a remittance including other checks, which totaled $19,198.02. (61) Just prior to this remittance and at the close of business on April 14, the Bank of California owed the U. S. National a balance of $1305.01. This remittance was sent on April 15 (63). After this remittance was received by the Bank of California, according to the books of *that bank,* the credit balance of the U. S. National in the Bank of California was $3642.20 (35). According to the books of the U. S. National, the balances of that bank with the Bank of California on the respective dates were as follows:

April	15,	$11,837.49
"	16,	16,617.87
"	17,	14,198.76
"	18,	13,391.95
"	19,	Sunday
"	20,	3,070.37
"	21,	10,806.91
"	22,	5,745.25
"	23,	13,046.41
"	24,	8,641.24
"	25,	3,567.35
"	26,	Sunday
"	27,	592.40

On April 28 the account was *overdrawn* and the U. S. National *owed* the Bank of California $6469.28.

This credit balance from April 15 to April 28, with the Bank of California was utilized by the U. S. National in its ordinary course of business. The remittance sheets during that period showed that *none of the balance was transferred to reserve agents.* (65) Remittance sheets of the Bank of California to the U. S. National between the dates of April 14 and April 28, when the credit was exhausted (defendant's Exhibit B, 37), showed that the balances in favor of the U. S. National with that bank were utilized by the California bank's honoring checks drawn by depositors of the U. S. National, and in some few instances, indicated by numeral, the transfer of credits to other banks, for instance, the National Bank of Tacoma on April 13, honored a number of checks drawn on the U. S. National and forwarded them to the U. S. Na-

tional. In exchange for this remittance or collection by the Tacoma bank, the U. S. National sent to the Tacoma bank a draft on the Bank of California in payment of these items. The amount of this draft, which was dated April 15, was $6340.55. (65). The letter "U" on the remittance sheets indicated checks drawn on the U. S. National and cashed by the Bank of California (45)

Security State Bank checks. Two checks, aggregating $5363.06, drawn by the county treasurer on the Security State Bank of Chehalis, payable to the order of the U. S. National. These checks were sent by the U. S. National to the drawee bank in a remittance which aggregated $7767.22. Prior to this remittance the U. S. National owed the Security Bank a balance of over $13,000.00, and after this remittance the U. S. National still owed the Security Bank $5985.99. (61)

The U. S. National was declared insolvent by the Comptroller on September 21, 1914, and a receiver appointed that day. At the time of its failure there was actual cash in the vaults of the bank of $27,899.81. Between February 4 and the date of its failure, the lowest amount of cash and cash items in the vaults of the bank was, September 17, 1914, $23,-527.86. (53). From July 29 to the date that the bank

failed, there was deposited in the bank in actual cash by ordinary depositors, over its counter, $129,000. (68).

Mrs. McCormick sought to enforce a preferential payment to her of some $15,000.00, being the proceeds of all the warrants so collected by the U. S. National. The trial court eliminated from the plaintiff's claim to preference the amount of the two checks which were deposited by the U. S. National with the Security State Bank of Chehalis, aggregating $5363.96, and held as to that amount plaintiff was a general creditor. As to the balance of the proceeds of the collections above enumerated, passing to Coffman, Dobson & Co. and the Bank of California in Tacoma, the trial court allowed the preference.

Five other suits are pending against the insolvent, in which the respective plaintiffs are asserting preferential claims. (54). These five other suits involve $107,215.76. From that portion of the decree which allows Mrs. McCormick a preference of $10,-054.69, this appeal is prosecuted.

It will be observed that the questions presented by this appeal are limited to the transactions of the U. S. National with the Coffman, Dobson Co., and the Bank of California at Tacoma.

SPECIFICATION OF ERRORS.

1. The District Court erred in finding and adjudging that the deposit of the plaintiff's warrants with the defendant bank for collection and remittance was sufficient to establish a trust relation between the plaintiff and defendant bank on the bank's failure to remit the proceeds of such warrants when collected, and not merely a relation of debtor and creditor.

2. The District Court erred in ordering and directing the defendant, A. R. Titlow, Receiver, to pay to the plaintiff the sum of $10,054.69, or any other sum, as a preferred claim, out of the assets of the bank.

3. The District Court erred in rendering a decree allowing a preferred claim to the plaintiff in the sum of $10,054.69, which decree is contrary to the testimony and against the law, because the equities of the case entitled the defendants to a decree of dismissal.

ARGUMENT.

The right of Mrs. McCormick to receive a preferential payment out of the assets of the insolvent bank to the detriment of the general creditors must be based upon the principle that the proceeds of the collection of her warrants formed a trust fund, and that this trust fund was directly traceable into the assets which passed to the receiver.

It will be recalled that these warrants were purchased by her in August 1913. She returned them to the bank *for collection.* There were no instructions *to collect and remit.* At that time she was dealing with a perfectly solvent bank, and she dealt with the bank according to the custom which prevails among bankers.

In February and April, 1914, the bank collected the warrants. In September, 1914, the bank failed, never having accounted to Mrs. McCormick for the collections so made. As long as the bank held the warrants *uncollected,* the relation between McCormick and the bank was that of principal and agent, but according to banking custom, of which the court will take judicial notice, as *soon as collection was made,* the relation between Mrs. McCormick and the bank

was that of debtor and creditor. It is conceded that there were no *specific instructions* given the bank by Mrs. McCormick. The warrants were sent "for collection." Therefore she *impliedly* consented to deal with the bank according to customary banking methods.

What would be the ordinary, and customary way for the bank to account for the proceeds of this collection? Surely it was never contemplated by either Mrs. McCormick or the bank that when these warrants were called, the banker would go over and secure the actual cash for them, hold it separate and apart, and remit the actual money so collected to Mrs. McCormick. She lived in Tacoma. The bank was in Centralia. The court would have to strain the usual methods pursued between a bank and its customers in order to say that it was contemplated by the parties that the specific money collected for these warrants was to be remitted to Mrs. McCormick. When she deposited them with the bank for collection, *she impliedly consented* that *when collected,* the bank might remit to her out of a general mass of moneys that it had. This might be by cashier's check or by New York or Tacoma draft. There can be no doubt, that either method of remittance would have been satisfactory to Mrs. McCormick, as long as the bank remained solvent.

The trouble is that none of the parties contemplated that the *bank would fail.* Had the bank continued as a going concern, and had made the collection, could Mrs. McCormick have sued the bank for conversion for not accounting to her for the proceeds of the collection? Or would her action have been one for money had and received? Clearly the latter. Many courts have been thrown into confusion by attempting to trace a trust fund, when *in fact no trust fund existed.*

The discussion of this case is based on

(a) That there was no trust fund; and

(b) If there was a trust fund, it has not been established and identified as against the receiver.

No Trust Fund.

If it is established in this case that the relation between Mrs. McCormick and the bank was that of debtor and creditor, it is useless to pursue this subject further. If she is a creditor of the bank, she is like any other creditor who has deposited his good money and who in turn expected to receive payment in full. There is nothing in the nature of the case that makes the collection on the warrants any different from any other collection item which may be sent a bank. A person may deposit warrants for

collection, or he may deposit a note, or a check. The same legal principle underlies all collection items. The depositor *impliedly entrusts the proceeds of the collection with the bank,* and consents that after the collection has actually been made, the proceeds may be credited on the books, and a *similar* amount, but not the same amount, remitted.

In *Marine Bank* vs. *Fulton Bank,* 2 Wallace 252, the instructions were to "please hold the avails of the collection I have sent you subject to my order, and advise the amount credited."

The court recognizes the distinction between the relation of principal and agent and that of debtor and creditor. Mr. Justice Miller says at page 256:

"All deposits made with bankers may be divided into two classes, namely, those in which the bank becomes the bailee of the depositor, the title of the thing deposited remaining with the latter, and that other kind of deposit of money peculiar to banking business, in which the depositor for his own convenience parts with the title to his money and loans it to the banker, and the latter, in consideration of the loan of money and the right to use it for his own profit, agrees to refund the same amount, or any part thereof, on demand. The case before us is not one of the former class. It must be of the latter. The parties seem to have taken this view of it. * * * But the truth undoubtedly is, as stated in the second branch of the proposition, that both parties understood that *when the money was collected, plaintiff was to have credit with the defendant for the amount of the collection, and that defendant would use the*

money in his own business. Thus the defendant was guilty of no wrong in using the money, because it had become his own. It was used by the bank in the same manner that it used money deposited with it that day by city custom, and the relation between the two banks was the same as that between the Chicago bank and its city depositors."

This case is cited and approved in *Commercial National Bank* vs. *Armstrong,* 148 U. S. 50, in which Justice Brewer says:

"That reasoning is applicable here. Bearing in mind the custom of banks, it cannot be that the parties understood that collections made by the Fidelity during the intervals between the days of remitting were to be made special deposits, but on the contrary it is clear that they intended that the moneys thus received should pass into the *general funds of the bank* and be used by it as other funds, and that when the day for remitting came, the remittance should be made out of such general funds."

As long as these warrants remained with the bank uncollected, the bank was Mrs. McCormick's bailee. Had the bank during that period misappropriated the warrants, it would have been guilty of a conversion. After the warrants *were collected* and the proceeds turned into the general mass with other deposits, would it have been possible to say that any money embezzled from the bank was the actual proceeds of the McCormick collection? Mrs. McCormick selected the bank as a collecting medium because she considered it the most convenient and

practical way of effecting the collection. Had she desired to insure herself against all loss, she might have sent a special messenger to make the collection and bring her back the gold coin. This, however, she did not see fit to do, but used the ordinary business channels.

In *Freeman's National Bank* vs. *National Tube Works,* 151 Mass. 413, the court said:

"One who collects commercial paper through the agency of banks must be held impliedly to contract that the business may be done according to their well known usages, so far as to permit the money collected to be mingled with the funds of the collecting bank. *Dorchester Bank* vs. *New England Bank,* 1 Cush. 177. When a payment is made to his agent and the money is put with money of the collecting bank, he has a right to receive a corresponding sum, but he loses his right to the specific fund."

Your Honors have said:

"There is no recognized ground upon which equity can pursue a fund and impose upon it the character of a trust, except upon the theory that the money is still the property of the plaintiff. 'If he is permitted to follow it and recover it, it is because it is his own, whether in the form in which he parted with its possession or in a substituted form." *Spokane County* vs. *First National Bank of Spokane,* 68 Fed. 979.

In *First National Bank of Richmond* vs. *Wilmington,* 77 Fed. 401, C. C. A. 4th Cir., the draft was

sent "for collection." It was again forwarded for collection and remittance. The two banks had no mutual account. That court said:

"In Armstrong vs. Bank, 148 U. S. 50, the agreement was that the bank should collect for the plaintiff and remit every ten days, and the United States Supreme Court held that as soon as the paper was collected, the bank became a debtor to the plaintiff for the amount collected. This was equivalent to holding that on collecting the proceeds of drafts, the bank ceased to be an agent and bound to remit the very money collected, but became a debtor for the sum collected. The custom of banks does not require a collecting bank to keep money collected separate from other matters in its possession and to remit that very money to the bank for which it made the collection; and the courts will take judicial cognizance of this fact. If this were not so and if the payor and drawee of a draft were bound to look to the transmission of the very money paid upon it, an important branch of the business of banks would be discontinued, and the sending of money by express would become necessary in all cases of collections, to the great inconvenience of bankers."

In *Philiadelphia National Bank* vs. *Dowd,* 38 Fed. 172, the paper was indorsed *"for collection and immediate return,"* and it was sought to impress a trust against the insolvent collecting bank. That court said:

"I have treated this case as one in which the plaintiff is entitled to be considered as a cestui que trust. I think that it is not entitled to be so considered, but ought to be treated as an ordinary creditor, because the money collected, or at least a large

part of it, was allowed to remain for several months with the defendant bank. As I understand the course of business among banks in regard to collections of this kind, it is not expected that the *same moneys that are collected shall be forwarded.* On the contrary, they are uniformly treated as the money of the ordinary depositors, and are remitted by means of the system of exchanges of credit which forms a part of the general mercantile business of the country. The result of giving such collections a preference over ordinary debts of a bank would be to make national banks preferred creditors in every case of insolvency of other national banks."

Now, when a claim to priority is based upon a collection once made, there is no special fund created, according to the universal custom adopted for the mutual convenience of all parties. The collection is commingled with the other deposits of the bank, *unless the banker has received special instructions to preserve the fund and to transmit it in some other method than by check or draft.*

In *Merchants' & Farmers' Bank* vs. *Austin,* 48 Fed. 25, the court said:

"It is common every day business for banks to employ each other as collecting agencies and they perform this duty in no exceptional way, but in the same manner in which they do the general business of the bank. A bill is collected by the bank and the proceeds commingled with the general assets, so as to be entirely undistinguishable and with no earmarks or means by which it can be traced into any new investment. The bank breaks. Now on what principle does he stand on other or higher ground than he who with

the faith in the solvency of the bank deposits his money and loses it? The contention here is not supported by sound reason or authority. * * * The complainant bank was a victim of this fraud as well as others who had all been alike misled and deceived by the apparent solvency and good credit of the bank. But in a legal or moral point of view, was the fraud any deeper or more flagrant upon the complainant than upon the other creditors of the bank?"

The Circuit Court of Appeals for the 5th Circuit had this question before it in *Annhaeuser Busch Brewing Assn.* vs. *Clayton,* 56 Fed. 759, in which a draft was sent "for collection and returns."

"There was no contract, express or implied, that the collection from Morris of appellant's account was to be a deposit of any kind, but it is clear that it was intended that the money received from Morris should be remitted in a reasonable time from date of collection. Appellant enclosed its draft on Morris to the McNab Bank for collection and return."

Rule in Washington. The law in the State of Washington is clear that whether the instrument is sent for *collection and remittance* or for *collection only,* the relation of *principal and agent ceases upon collection* and that of *debtor and creditor arises after the collection has once been made,* and that in case of failure of the collecting bank, the party sending the collection is a general creditor.

Hallam vs. *Tillinghast,* 19 Wash. 20. A draft was sent "for collection."

"There is no contention that there was any agreement that the particular money should be preserved in specie. In fact, it must be presumed, under the custom stated, that the particular money paid to satisfy the draft was never received by the bank here, as following the custom the draft would be sent by the bank to its correspondent where the draft was payable, for collection. When paid, under such custom the specie would not be remitted, but the bank sending the draft would be credited with the amount merely, and such matter left for future settlement in the balancing of accounts. The respondent was bound to know this custom. The fact that he never specially agreed to deposit the proceeds of the draft with the bank made no difference. *If he wanted to except it from the general custom, there should have been an agreement that the specific money should be set aside for him or disposed of in some particular way, or at least that upon the payment of the draft a like amount should be segregated from the general funds of the bank and kept for him, thus keeping the proceeds in a specially substituted form.* Had this been done prior to the insolvency of the bank, no doubt a trust would have resulted as against the receiver, *if the particular proceeds in either the original or substituted form came in his possession.* There is no equity in a rule giving such claims as the plaintiff's a preference over general creditors. He trusted the bank under the general custom and deposited the draft for collection *the same as any other general creditor trusted the bank.*"

It must be conceded that there are authorities to the contrary, but it is submitted that the well reasoned cases recognize the distinction between the relation of the parties as long as the item is uncollected, and the relation that arises upon the collection's being made.

Federal Court will follow the State law. This transaction occurred in the State of Washington, and in her dealings with the bank Mrs. McCormick *is bound by the decisions of the State court.* Mrs. McCormick lived in Tacoma, the bank was in Centralia and the collection made in Chehalis. All parties were dealing in the State of Washington.

In *Kent* vs. *Dawson Bank,* Fed. Cases 7714, 13 Blatchf. 237, a draft was drawn on a person in North Carolina. It was owned by a Chicago bank and transmitted by mail to the defendant in North Carolina with instructions to collect and remit the returns. The draft was collected through the B. & G. Bank. The collecting bank, after making the collection, failed before remitting the amount.

"The place of performance of a contract is generally a controlling consideration by which to determine the lex loci contractus, and where, as here, the contract was both made in North Carolina and was to be performed there, it is clear that the case must be controlled by the law of that State. It is not claimed that any statute exists in the State of North Carolina which affects the rights of the parties, or that the courts of that State have passed upon the direct question here, but the testimony of experts, lawyers of that State, has been produced, by which it appears that the question is yet an open one, to be determined by the general principles of commercial law, as recognized by that State in common with the other States of the Union."

Failure of Mrs. McCormick to Trace Any Trust Fund Into the Possession of the Receiver.

It is the settled doctrine of modern equity jurisprudence that a trust fund will be followed so long as it can be identified and traced either into property or into a larger fund held by a receiver. If the receiver has in his possession a fund which belongs to the claimant, it should be returned. It is immaterial whether the trust fund arose from a breach of contract for holding a special deposit or from a deliberate fraud. The early equity rule was that money could not be traced at all after it had been mingled with other funds of the trustee.

Ex parte Dale & Co., L. R. 11 Ch. Div. 772.

This rule has been modified by modern decisions. But in applying the modern rule, three principles must not be overlooked.

1. That *general creditors* cannot be held to atone for the omissions of a trustee. They are not to be punished for his wrongdoing. If the money has been taken and squandered, the *cestui que trust* becomes a general creditor and shares with the others, under all insolvent laws providing for the ratable distribution of assets.

2. Creditors who would otherwise be general ones, should not be allowed to profit by a breach of trust or fraud of the trustee.

3. One seeking to establish a trust fund must do so by clear and convincing proof. The burden of establishing and tracing his res, either in the original or in a substituted form, rests at all times upon the claimant.

If a national bank fails having $30,000 in cash, and it appears that within three months prior to its failure some $130,000.00 in actual cash had been deposited by general creditors over the counters of the bank, would it be possible for the court to say, in the absence of any specific proof, that a claimant to a fund of $15,000, which was obtained by the bank some *eight months prior,* could trace his money into the $30,000.00 remaining at date of failure? Is it not more likely that the $30,000.00 fund was received from the *later depositors?*

Coffman, Dobson & Co. account. Let us now apply these principles to the case at bar. When the warrants were paid, the bank received no *actual cash.* The county treasurer's check of February 4 on Coffman, Dobson represented approximately $1500 of the collection. This with other items was sent by the bank to Coffman, Dobson on February 6th, at which time Coffman, Dobson owned the U. S. National, including this item, about $5000. Of this, $1500 belonged to Mrs. McCormick.

What became of this credit with Coffman, Dobson? It was entirely exhausted on February 14. It is clear, under all the authorities, that no replenishment of the credit with Coffman, Dobson would *re-establish* any claim to a trust fund. *Our inquiry is therefore confined to the state of the Coffman, Dobson account between the date of remittance, to-wit, February 6th, and the date that the account was overdrawn on February 14.* The testimony shows that this credit was exhausted by Coffman-Dobson cashing checks which were drawn on the U. S. National by the latter's depositors. In other words, Coffman, Dobson paid certain debts of the U. S. National. These checks were of course transmitted to the U. S. National and charged to its various depositors' accounts and the checks returned. No part of this credit was transmitted to any reserve agents of the U. S. National (64). Both Coffman, Dobson and the U. S. National were *paying out money on each other's account. Neither was receiving any money on the other's account.* This credit account with Coffman, Dobson was utilized in the *ordinary course of business by the U. S. National in paying its debts and obligations to others. There is a total lack of proof that any part of this credit was traced either*:

(a) *Into the U. S. National bank vaults;*

(b) *Into anything of value which passed to the receiver.*

(c) *By transfer to any other bank through which the receiver ultimately received either money or any other item.*

Bank of California account. Practically the same facts existed as to the checks which were received in exchange for the warrants, and which checks were sent to the Bank of California in Tacoma. Here again it is apparent that *no cash* went into the vaults of the U. S. National. The two checks which went to the Bank of California, aggregating $8974.08, were included in a remittance of $19,198.02, but after applying this remittance of over $19,000.00, the Bank of California, *according to its own books,* was indebted to the U. S. National only to the extent of $3642.20. *In other words,* $5331,88 *of the two McCormick checks was therefore applied in extinguishing a debt at that very time* which the U. S. National owed the Bank of California, and in this respect the transaction with the Bank of California is similar to the transaction with the Security State Bank, in which instance the trial court held Mrs. McCormick not entitled to a preferenial claim because the check that went to *that bank* simply diminished the overdraft that the U. S. National had with it. In principle, what difference can it make whether the *overdraft is di-*

minished or entirely eradicated and a small credit balance established? Surely the claimant would lose his right to follow any trust fund beyond the *remaining balance.*

But let us go further. If we take the books of the U. S. National Bank, we find that after this remittance, the U. S. National had a credit balance with the Bank of California on April 15 of some $11,000., the credit balance remaining and fluctuating from day to day *until an overdraft occurred on April* 28. The discrepancy between the books of the two banks arises in the ordinary course of business in the following way: The U. S. National was like any other depositor in the Bank of California. The *depository's* books would show the *actual* condition of the account, the *depositor's* books showing outstanding items which *had not been actually credited* or *actually charged.* There is nothing mysterious about the deposit of one bank in another. The relation between the two banks is simply that of depositor and creditor, just the same as any customer of a bank. It is simply a question of balances, debits, and credits. (Testimony of Ralph S. Stacey for plaintiff, 50.)

What became of the balance that the U. S. National had with the Bank of California between April 15 and April 28, when the overdraft occurred? It

affirmatively appears that a substantial amount of this credit went to the depositors of the U. S. National (63). As to the remainder of the fund, the record, so far as it speaks at all upon the subject, shows that it was expended in the payment of other debts of the bank. None of this balance was transferred to other reserve agents of the U. S. National (65), and there is no showing that any portion of this *credit found its way into the vaults of the U. S. National.* The fact that the California bank was a reserve agent of the U. S. Bank is immaterial. Mr. Stacey's testimony shows that the relation between these banks under such circumstances is purely that of debtor and creditor. The reserve bank does not hold the funds sacredly set aside from the balance of its assets, but it is simply a debtor to any amount of the reserve credit shown on its books. As expressed in § 5192 of the Revised Statutes, it is merely *"a balance due"* from one association to another. Precisely the same principles apply as would obtain in case a trust fund had been traced into the hands of a private individual.

Mrs. McCormick then is driven to inferences and conjectures in order to establish her right to preference. She says: "The proceeds of my warrants went in the form of a credit to some of your correspondent banks. *It will be presumed* that this found its way back into your vaults and into the hands of

the receiver." Such a doctrine is antagonistic to practically all the decided cases on this subject. As said in *Beard* vs. *Independent District of Pella City*, 88 Fed. 375, p. 381:

> "Why should fiction be resorted to in order to sustain a preference on behalf of the school district to payment out of a fund not augmented in fact by any sum belonging to the district?"

Burden of Proof of Plaintiff.

Not only has the claimant in this case failed to establish by proof that the fund that she claims came into the possession of the receiver, but the record conclusively proves the contrary. Counsel point to the fact that at various dates the U. S. National had more than enough cash in its vaults to pay the complainant's claim. That might be material *if it were shown that the claimant's fund had been traced into the vaults of the bank.* The fact is that credit was traced into two depository banks and there dissipated. The defendant receiver has gone further in this case in the matter of proof than is necessary by showing that the proceeds of these credits were dissipated. The claimant is driven to the position of asserting a charge upon *all the assets of the insolvent bank,* a doctrine which is repudiated by all the authorities.

In the *City of Litchfield* vs. *Ballou,* 114 U. S. 190, the court said:

"If the complainants go after the money they let the city have, they must *clearly identify* the money or the fund or other property which represents that money in such a manner that it can be reclaimed and delivered without taking other property with it, or injuring other persons, or interfering with others' rights."

In this connection we call the court's attention to *Schuyler* vs. *Littlefield,* 232 U. S. 710, to which case we will have occasion to refer in detail in another portion of this brief.

Your Honors applied this doctrine in *In re Acheson Co.* 170 Fed. 427, in which case the claimant attempted to establish a trust fund against a bankrupt's estate:

"But it is a general rule, as well in a court of equity as in a court of law, that in order to follow trust funds and subject them to the operation of the trust, they must be identified. (Citing authorities.) In carrying out the rule, when it comes to *proof, the owner must assume the burden of ascertaining and tracing the trust funds,* showing that the assets which have come into the hands of the trustee have been directly added to or benefited by an amount of money realized from the sales of the specified goods held in trust, and recovery is limited to the extent of this increase or benefit. * * * So funds that have been dissipated or that have been used to pay other creditors, or that have been spent to pay current business expenses, are not recoverable, because they are gone and there is nothing remaining to be the subject of the trust."

In *Empire State Surety Co.* vs. *Carroll County,* 194 Fed. 593, C. C. A. 8th Cir.:

"It is indispensable to the maintenance by a cestui que trust of a claim to preferential payment by a receiver out of the proceeds of an estate of an insolvent, that *clear proof* be made that the trust property or its proceeds went into a specific fund, or into a specific, identified piece of property, which came into the hands of the receiver, and then the claim can be sustained to that fund or property only, and only to the extent that the trust proprety or is proceeds went into it. *It is not sufficient proof* that the trust property or its proceeds went into the *general* assets of the insolvent estate and increased the amount and value thereof which came into the hands of the receiver."

Claimant has not traced any trust fund into the hands of receiver.

With the burden resting upon Mrs. McCormick to trace and identify the proceeds of her collection either in the original form or in some substituted form, it is not sufficient that the claimant show a mere augmentation or swelling of assets, nor is she entitled to a lien against the *general assets* of the receiver. It is her duty to trace, by clear and satisfactory proof, the trust res in the receiver's possession. Some of the earlier cases, including those from this circuit, fell into error in this respect, as we will show later.

This general rule is stated in *Peters* vs. *Bain,* 133 U. S. 670, which was a suit to recover misap-

propriated trust funds. Bain & Company, a copartnership in control of the Exchange National Bank, had appropriated practically all the assets to their own purposes. That was a suit by the receiver of the bank to impress a trust on the assets of the partnership, which had assigned for the benefit of creditors. The property which was sought to be recovered fell into two classes, the first relating to property which was purchased with moneys that could be *identified* as belonging to the bank, and second, that which was bought and paid for by the firm out of a *general mass* of moneys in their possession, and which *may* or may not have been made up in part of what had been wrongfully taken from the bank. The trust was held established as to the first property, which was directly traceable to the assets of the bank. As to the second class the court said:

"Some of the money of the bank *may have gone into this fund,* but it was not distinguished from the rest. The mixture of the money of the bank with the money of the firm did not make the bank the owner of the whole. All the bank could in any event claim would be the right to draw out of the general mass of money, so long as it remained money, an amount equal to that which had been wrongfully taken from its own possession and put there. Purchases made and paid for out of a general mass cannot be claimed by the bank, *unless it is shown that its own moneys then in the fund were appropriated for that purpose.*"

In *Empire State Surety Co.* vs. *Carroll County*, 194 Fed. 593, C. C. A. 8th Cir., Judge Sanborn states four rules governing this class of cases:

"1. The claimant must prove clearly that the trust property or its proceeds went into a specific fund or specific property, which came into the hands of the receiver. It is not sufficient to prove that the trust property or the proceeds went into the general assets and increased the amount coming to the receiver.

"2. If trust funds are mingled in a common fund, and payment is made out of that fund, claimant can recover not exceeding the smallest amount the fund contained subsequent to the commingling, since the presumption is that the trustees kept the trust fund sacred.

"3. For this reason the legal presumption is that promissory notes and other paper coming into the hands of the receiver were not procured by the use of trust property.

"4. Where the property of many cestuis que trustent is mingled, and payment made out of the common fund, the presumption is that the moneys were paid out in the order they were paid in, and cestuis que trustent are entitled to preference in the inverse order of their payments into the fund. First in, first out."

That case involved various claims founded upon different facts. Judge Sanborn said:

"They next claim that they are entitled to preferential payment of about $12,000.00, first, because $4,455.05 was owing on the notes discounted by the bank between June 11, 1908, and October 17,

1908, which came to the hands of the receiver, but the claim to such an allowance on account of these notes is forbidden by the third rule and by the fact that there is no evidence tracing any of the county deposits or any of the proceeds of them into any of these funds; second, because the receiver collected $1,763.77 *from credits to the First National Bank in other banks,* but no preference on this account may be allowed for the same reason; and third, because $5,912.05 in cash came into the hands of the receiver when the bank failed, but the allowance of a preference on this account is forbidden by the fourth rule, and by these facts: All of the deposits of the county were made prior to October 10, 1908, except a deposit made on that day of tax receipts aggregating $1,041.22, and checks of third persons aggregating $486.11, and a deposit made on October 17, 1908 of $1,604.88 in checks. It was for these two deposits that the preference of $3,132.21 was allowed to the sureties by the court below. But this record has been searched in vain for any evidence that the checks for the $1,604.88 deposited on the last day the bank was open ever went into the hands of the receiver, and no claim is made to recover these checks, nor can any evidence be found sufficient to show what banks these checks were drawn upon, or that any moneys derived from them ever went into the $5,912.05 or into the hands of the receiver. Proof that these checks augmented the cash that went into the hands of the receiver, or that they produced cash which he obtained, was indispensable to any preference on their account. But checks of third persons on the bank with which they are deposited, which are paid by crediting the bank and charging the drawers on the books, fail to increase the cash in its possession, and form no basis for preferential payment to the depositor. *Beard* vs. *Independent District of Pella City,* 88 Fed. 375. Moreover, the deposit of checks of third persons which are credited to the depositor and used by the bank to pay its debts, bring

no money into its fund of cash, and form no foundation for preferential payment to the depositor. *City Bank* vs. *Blackmore,* 75 Fed. 771. Again checks of third parties, deposited with the bank credited to the depositor, and collected through a clearing house, lay no foundation for a preferential payment, in the absence of proof of the of them, for they may have been and usually are used, in whole or in part, to discharge the debts of the bank (citing authorities.) These checks may have been, and the probability is much greated than most of them were, used for some of these purposes than it is that cash for them was paid into the bank and remained there at the close of the day and went into the hands of the receiver."

An analogous case to the one at bar was that of *American Can Co.* vs. *Williams,* C. C. A., 2d Cir. 178 Fed. 420. Preference was claimed against the receiver of an insolvent bank on the following grounds: Plaintiff forwarded to the Fredonia Bank for collection certain drafts on two local corporations, aggregating some $28,000. The bank collected the drafts in the following manner: First, drafts paid by the drawees' check on outside banks, made payable to the Fredonia bank, and subsequently *paid directly to defendant as receiver.* Second, drafts paid by the drawees' checks on outside banks, made payable to the Fredonia bank, and paid by the former to the latter *before* the appointment of a receiver. Third, drafts paid by the drawees out of their accounts as depositors of the Fredonia bank. *Fourth,*

drafts paid by the drawees' checks on outside banks made payable to the Fredonia bank, and indorsed and delivered by it to the Merchants Exchange National Bank of New York City, and credited by such bank to the Fredonia bank.

Your Honors will perceive that the fourth state of facts is identical with those at bar.

It was further *conceded* in the case that

"At all times mentioned in the complaint prior to the 20th day of June, 1905, the assets of the Fredonia Bank and the assets which came into the defendant's hands as receiver and which are now in his hands, exceeded the amount of the plaintiff's claim."

The court assumed that the proceeds of certain of these drafts did come into the possession of the bank *before* the receivership *and constituted trust funds* in its hands, but the court says:

"The difficulty is, upon the agreed statement of facts, in following such funds into the hands of the receiver. *It may be* that prior to the receivership the bank used the trust fund to pay its debts with. It may be that these funds were wholly dissipated. *There is absolutely nothing to show that they had any connection with any of the property which came into the possession of the receiver.* The stipulated facts are wholly insufficient to show *any identity* of the property followed with the funds sought to be charged against it, or to show that the amount of

such property was increased or augmented by such funds. While the right to follow misapplied moneys as trust funds into the hands of a receiver has been extended in the modern decisions, there has never been in the federal courts a departure from the principle that there must be some identification of the property followed with the trust funds. * * * If the plaintiff's contention is well founded, that to follow misappropriated moneys it is only necessary to show that a receiver has, and that the trustee had, assets, the rule is simply that a demand for such moneys is a preferred claim against any substantial estate, and to adopt this view would do away with all the equitable principles out of which the right to follow trust funds grew."

In *City Bank* vs. *Blackmore,* 75 Fed. 771, C. C. A. 6th Cir., it appeared that the plaintiff City Bank sent a draft on August 24, to the Commercial National Bank of Nashville. The draft was drawn on Latham & Co., of New York, and was for $5,000.00. The Commercial Bank, then insolvent, received the draft August 25, credited the City Bank, and immediately sent the draft to the Bank of the Republic, its New York correspondent, to be deposited to the Commercial Bank's credit. Later in the day, August 25, the Commercial Bank was closed. The New York bank credited the draft to the Commercial Bank August 27. The City Bank stopped payment on the draft August 26. Accordingly the drawee refused to pay, but later, by direction of the City Bank, paid when the New York Bank brought suit

against the City Bank on the draft. The City Bank then presented a claim to the receiver and asked that $5,000 be allowed as preferred. Judge Taft, in holding the City Bank not entitled to priority, said:

"But the difficulty with the complainant's position is that neither the draft nor the proceeds of the draft have come into the receiver's hands. The sole question is therefore whether the *credit* thus secured by the Commercial Bank and its receiver by the draft entitles the City Bank to take $5,000 out of the assets held by the receiver. The question must certainly be answered in the negative in any view which can be taken, unless it appears that the assets were increased $5,000 by the credit, or that the claims against them were so decreased that there was $5,000 *more for distribution* among those who remained creditors after the credit than there would have been had no credit been given to the Commercial Bank for the draft. This does not appear. If no such credit had been allowed by the National Bank of the Republic, it would merely have been a claimant for $5,000 more and would have been entitled, not to $5,000 in full, but only to pro rata dividends on that amount. The benefit to the general fund from the draft, therefore, is limited to the amount of dividends payable on the $5,000.00, and that amount the receiver has already allowed to the City Bank. It has no ground for complaint, therefore. No authority has been cited to show that a claim founded on fraud is entitled to *priority* over other claims. It is only where, by rescission of the contract out of which the claim arises on the ground of fraud, that the specific thing parted with or its proceeds can be sufficiently identified to be returned, that fraud seems to give a priority of distribution."

The opinion was concurred in by Mr. Justice Lurton.

By depositing a check with a correspondent bank in the nature of things, does it make any difference whether the *debt to the correspondent bank* is reduced, or whether the credit with the correspondent bank is used to *pay other creditors?* In both instances the fund is lost. There is no greater amount for distribution among the general creditors. Instead of making A a creditor of the bank, B is made a creditor, and the substitution of parties is the only thing accomplished by the paper transaction. This question of tracing trust funds against an insolvent was recently before the Supreme Court in *Schuyler* vs. *Littlefield,* 232 U. S. 710. The same case in the lower court, *In re Brown,* 193 Fed. 24. In the Circuit Court of Appeals the facts appeared as follows:

The bankrupts, Brown & Co., had converted certain stock belonging to the Princeton Bank. From the proceeds of the stock, Brown & Co. deposited $1,120 in the Bank of Commerce and $280 in the Hanover Bank. These transactions were on August 17 and August 24. The bankruptcy occurred at noon, August 25. The bankrupts also sold other stock of the Princeton Bank, and on August 13 had deposited the proceeds, $1,787, in the Hanover bank. As to Brown & Co.'s deposits in the Bank of Commerce, it showed that there was a balance in favor of the bankrupts from August

17 to 24 largely in excess of $1,120. The balance August 25 was $21,000 but this was exhausted by checks subsequently presented. and the trustee received no money from that account. It further appeared that on August 25, though Brown & Co. had transferred $4,000 from the Bank of Commerce to the Hanover Bank by check, there was nothing to show that the $1,120 trust funds were included in this check and reappeared in the balance of $2,000, *which balance the trustee in bankruptcy received from the Hanover bank.* As to the deposit in the Hanover bank, the claim of the Princeton bank against this fund aggregated $280, plus $1,787, making a total of $2,067. The balance on the books of the Hanover Bank in favor of the bankrupts on and after August 13 to August 24 *were largely in excess* of the sums due the Princeton bank. It was held, however, that a trust fund was not established, that there was nothing to show that these balances represented the trust money of the Princeton bank rather than the trust money of various other persons urging similar claims aggregating $21,000. There was also nothing to show but that during the same day the balance had been entirely wiped out and the trust fund lost, and subsequent deposits would not make it good.

Your Honors will see the amazing similarity of the facts in the *Brown* case to those in the case

at bar. *First.* The insolvent was dealing with two correspondent banks, in which correspondent banks the trustee had deposited the funds in dispute. *Second.* The alleged trust fund was represented by mere credit balances due the insolvent. The *Brown* case contains these *additional* facts, which were *favorable* to the claimant. *First.* The fund of $4,000 had been transferred from one of the depositories to the other. *Second.* The trustee of the insolvent actually received in cash over $2,000 *after insolvency* from the second depository. As to the insolvent's account with the Bank of Commerce, that court said:

> "If $1,120 of the claimant's money was left in that bank, it has been dissipated and can be traced no further."

The claimant then asserted that by the transfer of the $4,000 from the Commerce bank to the Hanover bank, his trust fund was thereupon transferred to the Hanover bank, and that the trustees in bankruptcy admittedly received in cash the sum of $2,-055.97, this cash receipt included the claimant's $1,-120. That court said:

> "This seems a very tenous presumption *in the absence of any evidence to support it.* The amounts are different. There is nothing to show that there was a sum of $2,880 trust money of some sort with which the claimant's $1,220 was being shifted by the bankrupts, for some unexplainted reason, from one bank to another. As we said in *In re McIntyre,* Grace's appeal, 185 Fed. 96, 108 C. C. A. 540, while

the doctrine of following trust funds has been much extended in modern decisions, there has never been a departure in the Federal courts from the principle that there must be some identification of the property sought to be charged with the trust fund. * * * The special master finds that 'The opening and closing balances in the Hanover bank on and after August 13, were largely in excess of these (2 deposits), *but the finding is not sufficient.* There is no reason why it should be *assumed* that these balances were being reserved because they represented the trust money of the Princeton bank rather than because they represented the trust money of Simpson or Scrotton or any of the others similarly situated, enumerated above (aggregating $21,783.39), or indeed any of the other claimants who from time to time have appeared in this proceeding seeking to trace and recover for property converted by the bankrupt. Moreover, it is not enough to show that there was a morning and afternoon balance for several successive days large enough to cover that amount of money which was improperly converted. It might very well be that on any one day checks were presented which exhausted the morning balance and its accretions, in which event these moneys would have been dissipated. We are not prepared to assent to the proposition that subsequent deposits are to be taken as having been made to make good claimant's money thus drawn and spent. *Board of Commissioners* vs. *Strawn,* 157 Fed. 51."

This case was affirmed in the Supreme Court in *First National Bank of Princeton* vs. *Littlefield,* 226 U. S. 110. The same case was also before the Supreme Court of the United States as to another claimant *sub nom Schuyler* vs. *Littlefield,* 232 U. S. 710. In affirming the Circuit Court of Appeals, the Supreme court said:

"Money was paid by Brown & Co. to outsiders and to the bank. It would serve no useful purpose to make a detailed statement of the testimony. The evidence has been fully discussed by the court of appeals in considering this claim of the appellants, along with that of several other parties seeking, on somewhat similar facts, to trace trust funds into the bank, and thence into collaterals which ultimately came into the hands of the trustee. All these claims were disallowed because of the failure to make the requisite proof. Our investigation of the facts leads us to the same conclusion, as far as concerns the appellants' claim. They were practically asserting title to $9,600 said to have been traced into stock in the possession of the trustee. Like all other persons similarly situated, they were under the burden of proving their title. If they were unable to carry the burden of identifying the fund as representing the proceeds of their Interborough stock, their claim must fail. If their evidence left the matter of identification in doubt, the doubt must be resolved in favor of the trustee, who represented all of the creditors of Brown & Co., some of whom appear to have suffered in the same way. Like them, the appellants must be remitted to the general fund."

With the foregoing review of the decisions of the other circuits and the Supreme Court of the United States, let us now turn our attention to this circuit. We have already called the court's attention to the last decision of your Honors on this point in *In re Acheson,* 170 Fed. 427, in which case a preference claim was asserted by the petitioner for the proceeds of goods sent to the bankrupt on consignment. The petitioner alleged in that case that the trust fund was not kept separate and apart, but wrongfully mixed

with the other money of the bankrupt, and that it had been used in payment of the bankrupt's employees and other running expenses, and paying other creditors and in purchasing other goods, wares and merchandise, which composed the assets of the bankrupt. The question was whether this made a *prima facie* showing of a charge upon the funds in the trustee's hands in favor of the owners of the goods, and if so, to what extent did it reach?

"We do not mean to be understood as holding that equity will grant to a cestui que trust relief against any assets in the hands of a trustee, *for it will not go farther than to give a lien when the facts are that there remain in the estate specific funds or property which have increased the assets of the estate and which represent the proceeds of the specific property entrusted to the bankrupt.* So funds that have been dissipated or that have been used to pay other creditors, or that have been spent to pay current business expenses are not recoverable, because they are gone, and there is nothnig remaining to be the subject of the trust. This qualification of a general rule is to be applied to the facts pleaded in the present case, inasmuch as it is alleged that some of the trust moneys were used by the bankrupt in paying its employees and expenses of running its business and in paying other creditors. For them there can be no recovery."

In that case your honors cited with approval the earlier case of *City of Spokane* vs. *First National Bank,* 68 Fed. 982, and also other cases heretofore mentioned in this brief. In addition, your Honors relied upon the leading case of *Lowe* vs. *Jones*, 192

Mass. 94, 6 L. R. A., N. S. 487. In the *Acheson* case, this court adopted the universal holding of the other circuit courts of appeal, repudiating some of the earlier holdings in this circuit.

One of these early cases was *San Diego County* vs. *California National Bank,* 52 Fed. 59, where a trust was decreed against the general assets of the estate, without attempt to trace the fund.

In the subsequent case of *Multnomah County* vs. *Oregon National Bank,* 61 Fed. 912, the court expressly refused to follow the *San Diego* case. It was criticised in *In re Marsh,* 116 Fed. 396, and by Judge Lowell in *In re Mulligan,* 116 Fed. 715. Judge Gilbert in the *Spokane County* case, in 68 Fed. 979, 982, said that this case, among others, laid down a doctrine to which the court could not assent. It was followed by the lower court in the *Beard* case, 83 Fed. 14, which was reversed by the Circuit Court of Appeals in 88 Fed. 375. Judge Sanborn, in the *Carroll County case,* 194 Fed. 604, says that the doctrine of that case and some others is sustained "neither by reason nor authority."

Your Honors' decision in *Spokane County* vs. *First National Bank of Spokane,* 68 Fed. 979, is a leading case in this country on the right of a claimant to assert and follow an alleged trust fund. It has been

cited and its language quoted many times by other circuit court of appeals with approval. It has stood as a solid rock against all attacks. A circuit court in Ohio attempted to explain it: *Board of Commissioners* vs. *Patterson,* 149 Fed. 229, but the decision of the lower court was promptly reversed by the circuit court of appeals in the 6th circuit in *Board of Commissioners* vs. *Strawn,* 157 Fed. 49.

A case upon which Mrs. McCormick will rely is *Merchants' National Bank of Helena* vs. *School District,* 94 Fed. 705. In that case there was admittedly a trust fund, and the only question was whether it had been traced into the hands of the receiver. The claimant was dealing with a Helena bank, and his fund consisting of a collection item of $13,000 had been deposited to the credit of the Helena Bank with the National City Bank of Boston, which was the correspondent of the Helena bank. After this credit with the Boston bank, the Helena bank had a credit balance with that bank of over $39,000, *against which it drew on that day* the sum of $10,000, leaving a balance of some $29,000. A few days later a *draft* was drawn by the Helena Bank against the Boston bank of $8,000. Your honors said:

"The question is not complicated by any failure on the part of the Boston bank to pay to the Helena bank in full the amount which it received. *The Helena bank received the money in the due course of business.*"

In that case the actual money found its way into the Helena bank. If your Honors' decision in the Helena bank case means that the mere obtaining of a *credit* by the Helena bank with the correspondent bank is the receipt of the money, by the Helena Bank, we submit that the case can not be sustained on principle and is opposed to the overwhelming weight of authority. Suppose the Helena bank had been overdrawn at the Boston bank and the credit had been used to diminish the overdraft. Clearly the trust fund would be lost.

Now let us suppose that after the credit of the amount of the trust fund is obtained with the Boston bank, the Helena bank draws a draft on Boston *not to transfer the credit to its own vaults,* but to *pay a debt that the Helena bank owes A or another bank.* Is there any reason for saying, in such an instance, that the trust fund has not been dissipated, or that the assets in the hands of the receiver have been swollen and augmented. This would be directly contrary to your Honors' previous ruling in the *Spokane County* case. The Helena bank case has never been cited as sustaining any such principle, that is, that a credit with the correspondent bank for a trust fund is receipt by the bank itself, except in one case, which was on a *preliminary* hearing, *City of Centralia* vs. *Titlow, Receiver,* heard by the same trial judge as

this case. The *City of Centralia* case is now on appeal to this court. *City of Centralia* vs. *U. S. National Bank*, 221 Fed. 755.

Mrs. McCormick will say that "the receipt by the *agent* is a receipt by the principal. As soon as we trace this item into a correspondent bank we trace it into your actual possession." She will say that your Honors have so held in the Helena bank case. This overlooks the qualifications of the general rules of law applicable to of principal and agent as applied to a bank and its depositors. In a sense a bank is the agent of each of its depositors. It is also their debtor.

Counsel will be unable to cite to your Honors any case where a trust fund is sought to be followed that applies he principle of agency to a correspondent bank and which holds a *credit* with the correspondent bank is receipt of the fund by the bank itself. Such a doctrine would be antagonistic to all banking principles and interests. A bank in a large city is the correspondent and reserve agent of many other banks. It breaks. Is every bank that has a deposit in the city bank entitled to preferential payment of its claim as opposed to *all other depositors* in the bank? The depositing bank is in the same position as any other depositor, individual or otherwise.

In the Helena bank case, suppose it had been the Boston bank that had failed, owing the Helena bank more than the $13,000 deposited by the school district. Would the Helena bank have had a right to a preferential payment as against the Boston bank for the amount of the Helena bank's deposit?

We have called attention to the Helena bank case for the reason that the lower court gave it the strain- of this court in he Spokane County case, and the subsequent decisions by the same court, and with the overwhelming weight of authority elsewhere, than the narrow construction attempted to be placed upon the case by the appellee and the trial court.

It is preferable to give it that construction which renders that case consistent with the prior decision case consistent with the prior decision of this court in the Spokane County case, and the subsequent decisions by the same court, and with the overwhelming weight of authority elsewhere, thaa the strained construction attempted to be placed upon the case by the appellee and the trial court.

Banking business is done by means of debits and credits. If the insolvent bank, through the misappropriation of a trust fund, obtains a credit with the correspondent bank, and that credit is returned in money to the insolvent bank or goes to purchase notes or other securities which pass into the hands

of the receiver, the trust fund is traced, but if the credit balance with the correspondent bank is exhausted or utilized in the ordinary course of business by the insolvent bank, if it pays creditors of the insolvent bank, running expenses, or other charges gainst it, the fund is lost. There can be no *presumption* that the receipt by the correspondent bank carries the fund into the vaults of the insolvent bank and to its receiver, for, as we have seen, the burden of *actually tracing* the fund is upon the claimant.

In addition to the cases heretofore cited, we call the court's attention to the following authorities bearing on this subject and the right to trace funds. Many of these cases involve credits obtained with correspondent banks and reserve agents, and hold that the receipt of a credit with a correspondent bank is not a receipt by the bank itself when it comes to asserting a preferential claim.

Lucas County vs. *Jamison,* 170 Fed. 338;

In re See, 209 Fed. 172, C. C. A. 2d Cir.

In re Brown, 193 Fed. 24, C. C. A., 2d Cir. Affirmed *sub nom* Schuyler vs. Littlefield, 232 U. S. 710.

Cherry vs. *Territory,* 89 Pac. 190 (Okla.)

In re Dorr, 196 Fed. 292.

Rule of first in first out. It appeared that there were five other pending suits against this bank and its receiver asserting preferential claims as follows:

City of Centralia for $44,553.09, which was deposited in July 1914.

Continental & Commercial National Bank, for $5166.67, covering a collection in August 1914.

Frank P. McKinney, as receiver, for $36,550.00, for preferential claim covering a transaction in August 1914.

Nicholas Petrinovich, covering a deposit of $150.00 on September 15, 1914.

John P. Sundquist, covering a deposit of $1,-296.00 on August 31, 1914. (54-56)

So that in addition to the suit at bar, there were pending at the time of trial of this case other suits involving over $80,000 of alleged preferential claims against this bank. All of the other claims covered transactions subsequent to May 1914. It will be recalled that Mrs. McCormick deposited her warrants in 1913. They were *collected* in February and April 1914. Mrs. McCormick's claim is therefore the first in order of time. When the bank closed there was actual cash on hand of $27,899.81 (53). From July 29 till the date that the bank closed there was some $129,000 in actual money deposits which passed over the counter of the bank. Again we are thrown into the realm of mere speculation as to whom the cash on hand at the date of insolvency belonged to. Did it

belong to the $129,000 of general depositors, subject to ratable distribution among them, or did it belong to Mrs. McCormick, who alleges a breach of trust on the part of the bank not later than April 1914, or does it belong to the City of Centralia, by reason of its transaction in July, 1914? The rule is that when the property of many beneficiaries is commingled and payment is made out of this fund, there is a presumption that the moneys that were paid out were paid out in the order in which they were paid in, so that the beneficiaries are entitled to preference in the *inverse* order of thier payments into the common fund. As said in *Empire State Surety Co.* vs. *Carroll County,* 194 Fed. 593 at p. 607:

"All these deposits were trust funds, and applying the rule that deposits of equal trust rank are presumed to be drawn out in the order that they were paid in, and that allowable preferences in the remaining balance must be given in inverse order of their payment to the trustee, all of the deposits of the 10th of October had been drawn out long before October 17, 1908, and the $5912.05 was the property of the *later depositors.*"

In *Lucas County* vs. *Jamison,* 170 Fed, 338, the court said:

"But the court knows that there is still another on its docket in which a preference of more than $100,000 is asked; so it will be seen that if preferences could be allowed in these cases, then the other cases involving so large an amount might cover the same funds."

In *Cherry* vs. *Territory,* 89 Pac. 190 (Okla.) which is in other respects pertinen, he court said:

"But when the evidence in the particular case shows affirmatively that a party stands in the same position as others, as for instance in a receivership matter, and the court is passing upon the priority of claims, it should consider the effect of the particular judgment upon the other creditors similarly situated."

While there is a showing that there was a certain balance due from correspondent banks when the bank failed, still these amounts are not segregated, and the whole balance, as far as this claim is concerned, might be owing from the Bank of California. Surely any balance that was owing from that bank could not be taken into consideration, because the right to follow the *credit* in the Bank of California ceased when the overdraft occurred with that bank on April 28, 1914. The whole amount due from correspondents might be from Coffman-Dobson, but for a like reason *that account* could not be counted, because an overdraft occurred with Coffman, Dobson & Co. on February 14, 1914, and any credits in that account subsequently, as has been shown, would not replenish the fund. From all that appears, sums due from other correspondents may be subject to offsets and counterclaims.

Form of Decree. This decree fails to take into account any of the other pending suits for preference.

Judgment is given against the receiver Titlow for $10,054.69, and he is directed to pay that out of the moneys in his hands. This form of decree is objectionable first as being a judgment against the receiver, and second as failing to take into consideration other preferential claims asserted against the bank. *Denton* vs. *Baker,* 79 Fed. 189; *Richardson* vs. *Louisville Banking Co.,* 94 Fed. 442.

Respectfully submitted,

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